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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

No. 1

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

vs.

ENGINEERS PUBLIC SERVICE COMPANY, *et al.*

No. 2

ENGINEERS PUBLIC SERVICE COMPANY, *et al.*,
Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA.

BRIEF OF DENIS J. DRISCOLL AND WILLARD L. THORP, TRUSTEES OF ASSOCIATED GAS AND ELECTRIC CORPORATION, DEBTOR, *AMICI CURIAE.*

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The Question to Be Argued.

This brief is directed only to the holding of the Securities and Exchange Commission, sustained by the United States Court of Appeals for the District of Columbia, that the "Virginia Gas System" is not retainable as an additional system together with the "Virginia Electric System"[1] under the Public Utility Holding Company Act

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[1] These gas and electric properties are not owned or operated by two separate operating companies. According to the brief of Engineers Public Service Company (p. 117) the gas and electric properties at Norfolk, Virginia, have been owned by the same operating company, Virginia Electric and Power Company, since 1930.

of 1935.[2] It is our position that the decision of the Commission in this case is bottomed upon a clearly erroneous interpretation of Clause (A) of Section 11(b)(1) of the Act.

The specific interest of the Trustees of Associated Gas and Electric Corporation in the question to which this brief is addressed arises from the fact that in the Associated Gas and Electric Corporation Holding Company System, there are several important subsidiary companies, which render both electric and gas service, and which are involved in a proceeding pending before the Commission under Section 11(b)(1) of the Public Utility Holding Company Act of 1935.

The more important of these companies, and their gross revenues from electric and gas service for the year ended December 31, 1944, are as follows:

	Year ended December 31, 1944	
	Electric Revenues	*Gas Revenues*
Rochester Gas and Electric Corporation	$14,243,641.00	$5,510,032.53
New York State Electric & Gas Corporation	27,265,704.76	4,113,363.31
Jersey Central Power & Light Company	12,698,759.92	3,113,134.25

Section 11(b)(1) directs the Commission to permit a registered holding company to continue to control one or more "additional * * * systems" if the standards of clauses (A), (B), and (C) are met. Clause (A) reads as follows:

> "Each of such additional systems cannot be operated as an independent system without the loss of substantial economies which can be secured by the retention of control by such holding company of such system;"

The crucial words are "the loss of substantial economies". This brief will discuss the use of these words in Clause (A) and the proof required to establish the loss

[2] 49 Stat. 803; 15 U. S. C. A. §79, hereinafter referred to as "the Act".

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of such economies upon severance of a gas system claimed to be retainable as an additional system together with a principal electric system.

It is at least doubtful whether Clause (A) is applicable to the situation presented by this case in view of the fact that the gas and electric properties here involved are owned by the same operating company. Section 1(c) of the Act declares the policy of the Act, in accordance with which all of its provisions are to be interpreted, to be "to meet the problems and eliminate the evils as enumerated in this section, connected with public utility holding companies." Ownership of gas and electric properties within a single state by one operating company is not one of the enumerated evils; nor does Section 1 of the Act list as one of the abuses which the Act was designed to remedy the combination of gas and electric services in the same holding company system. Moreover, a Congressional intent not to disturb State regulation of operating companies is evident from various sections of the Act, particularly Sections 8 and 9(b)(1). However, in the balance of this brief we shall assume *arguendo* that Clause (A) is applicable to the particular facts of this case.

The Importance of the Question.

The question here discussed is of vital public interest. The report of the Public Utilities Division of the Securities and Exchange Commission for the year 1944[3] lists 43 registered public utility holding company systems. Of these 43 systems, 32 conducted both electric and gas service, and had operating revenues from these services of $1,818,009,710 and $525,529,809, respectively. In many communities combined electric and gas service is furnished by such systems either through a single so-called "combination" operating company furnishing both services, or through separate companies.

In one early case in which the question came before it, the Commission found that a combination of gas and

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[3] Financial Statistics for Electric and Gas Subsidiaries of Registered Public Utility Holding Companies (1944).

electric properties constituted "a single integrated system" under Section 2(a)(29)(A) of the Act.[4] However, since that decision, the Commission has consistently held that a combination of gas and electric properties cannot constitute a single integrated system;[5] that, therefore, whether or not the combination can continue must be determined by reference to the standards for the retention of "additional systems", particularly Section 11(b)(1)(A). The question has been before the Commission under Clause (A) at least four times,[6] but in no instance has the Commission found compliance with the clause. Indeed, there are only two instances where the Commission has allowed the retention of additional systems. One such instance involved only electric properties[7] and the other involved only gas properties.[8] In these cases the Commission construed the words "loss of substantial economies" in a manner inconsistent with its decision in this case and with its argument in its brief before this Court. The inference is compelling that by its interpretation of Clause (A) in this case, and in every other case involving the combination of gas and electric properties, the Commission has sought to compel separation of such properties, even though owned by a single operating company, by setting up a standard for retention of additional systems which cannot possibly be met by any combination of gas and electric properties.

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[4] *American Water Works and Electric Company, Inc.*, 2 SEC 972 (1937).

[5] *Columbia Gas & Electric Corporation*, 8 SEC 443 (1941); *The United Gas Improvement Company*, 9 SEC 52 (1941); *Standard Power and Light Corporation, Standard Gas and Electric Company*, 9 SEC 862 (1941).

[6] *Engineers Public Service Company* (HCA Release No. 3796; September 17, 1942); *Middle West Corporation* (HCA Release No. 5606; February 19, 1945); *North American Company* (HCA Release No. 5707; April 9, 1945); and *Peoples Light and Power Company* (HCA Release No. 6000; August 23, 1945).

[7] *Federal Light and Traction Company* (HCA Release No. 4960; March 31, 1944).

[8] *Columbia Gas & Electric Corporation* (HCA Release No. 5455; December 1, 1944).

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Outline of Argument.

I. The Commission has made an unwarranted assumption that the effects of independent ownership of gas and electric services are *necessarily* beneficial.

(a) The Commission has proceeded in this case on the assumption that the effects of independent ownership of gas and electric properties are necessarily beneficial.

(b) The Act raises no presumption that independent ownership of gas and electric services would have "beneficial effects".

(c) There is no basis in fact for an inference that the effect of independent ownership of gas and electric services is *necessarily* beneficial.

II. Clause (A) as interpreted by the Commission prescribes a vague and meaningless standard.

(a) Congress intended Clause (A) to afford a definite, concrete and effective standard for the guidance of the Commission and the companies.

(b) The Commission has erroneously read into Clause (A) a type of limitation on the extent of holding company systems which Congress provided for only in Clauses (B) and (C).

(c) The Commission has been inconsistent in its interpretation of the words "substantial economies".

III. The Commission cannot refuse to find "the loss of substantial economies" on a basis *dehors* the record before it.

Argument.

I. The Commission has made an unwarranted assumption that the effects of independent ownership of gas and electric services are *necessarily* beneficial.

(a) The Commission has proceeded in this case on the assumption that the effects of independent ownership of gas and electric properties are necessarily beneficial.

The Commission has taken the position that in any determination with respect to "the loss of substantial economies" through severance of gas and electric services the "beneficial effects of independent ownership" must be assumed.[9] According to the Commission, these "beneficial

[9] At page 18 of its Findings and Opinion in this case, the Commission stated:

> "in measuring the loss of *economies* accompanying the severance of a combination of two utility systems, it is particularly important to consider the beneficial effects of independent ownership upon the efficient operation of each system. A consideration of increased expenditures alone does not adequately reflect the impact of the severance upon the two systems. Where, as here, gas and electric operations are conducted in the same territory and in many ways compete with each other, the danger exists that under a single management one business may be suppressed in favor of the other or that one will bear burdens properly allocable to the other."

The Court of Appeals of the District of Columbia in sustaining the Commission declared (138 F. (2d) 936, 944):

> "It is our belief that the Commission could not legally 'permit' the continued control of 'Virginia Gas' by 'Virginia Electric' unless it could be found from the evidence adduced at the hearing:
>
> "(a) That there would be a continuing substantial strength, enjoyed by the controlled company which it would not have under its own control.
>
> "(b) That there would be in the situation no reasonable expectation that a compensating strength would not be enjoyed by reason of its own control.
>
> "(c) That such continuing strength would not entail a sacrifice upon the part of the controlling utility.
>
> "In short, we are of the opinion that the mere showing of a material savings in operational expense (which, to some extent at least, would normally be expected) does not necessarily show the over-all situation."

It may be noted that the Court of Appeals refers to "Virginia Electric" and "Virginia Gas" as the "controlling" and the "controlled" companies, which is, of course, a fiction.

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effects" arise because in the case of combined gas and electric operations there are (1) "the danger * * * that under a single management one business may be suppressed in favor of the other" and (2) "the danger * * * that one will bear burdens properly allocable to the other".

At page 86 of its brief, the Commission asserts that:

> "the possibility of growth of the gas system might well be enhanced when it is freed of the same control as the larger and more remunerative electric system."

If the Commission has in mind aggressiveness of management in promoting the business, here again the Commission has made an assumption. If any assumption can reasonably be made, it is that any progressive management will endeavor to fully exploit all the possibilities of a business within economic limits. In the absence of positive evidence of failure by the existing management, whether some unknown future management would be likely to be more successful can only be guessed. Similarly, whether under independent operation both services will benefit or one service will benefit at the expense of the other or both services will suffer, can only be guessed.

In no case has the Commission attempted any proof of the alleged "beneficial effects of independent ownership", with the possible exception of the *North American* case (HCA Release No. 5707; April 9, 1945).[10] The Commission simply assumes that the "effects of independent ownership" will be "beneficial". The practical effect of this assumption is to place upon the Company an insuperable burden, namely to present evidence satisfactory to the Commission as to a matter which the Commission itself

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[10] In that case the Commission apparently placed some reliance upon a comparative statistical study of certain phases of the operation of independent gas companies, as against gas departments of combination companies, although in a case decided a month earlier involving the same holding company but different properties, the Commission had in effect rejected this type of evidence. *North American Company* (HCA Release No. 5657; March 15, 1945).

declares to be "not readily susceptible of absolute proof".[11] Thus the assumption becomes tantamount to an irrebutable presumption.

(b) The Act raises no presumption that independent ownership of gas and electric services would have "beneficial effects".

In its final report to Congress in connection with its study of the public utility industry, the Federal Trade Commission made the following recommendation (Final Report of The Federal Trade Commission to the U. S. Senate; 70th Congress, 1st Session (Senate), Document 92; Part 84-A, transmitted to the Senate on December 31, 1935, p. 617):

> "5. *Divorcement of Gas and Electrical Utilities*—Because of the fact that gas and electricity are increasingly competitive and in many communities are the two chief sources of power and light, and because 3 of the 4 dominant interests in natural gas and gas pipe lines also are in the electrical-utility field, it seems obvious that such double control presents a problem meriting serious consideration. The Commission therefore recommends that, with proper limitation as to time and place, divorcement of the two be made compulsory."

Although much of the data on which this recommendation was based had been transmitted to Congress from time to time (Report p. VI), and thus was available for congressional consideration prior to the passage of the Act, no version of the bill at any time contained any general prohibition against combination of gas and electric services. The only prohibitions related specifically to the following two matters: (1) a registered holding company or a subsidiary thereof was prohibited from having any interest, direct or indirect, in any company owning or operating capital assets for the transportation of natural gas in interstate

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[11] Commission Brief, page 90.

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commerce or for the production of natural gas; (2) the bill made it unlawful for any holding company to have any interest, direct or indirect, in "an electric utility company or a gas utility company serving substantially the same territory whenever the applicable State Law prevents or requires approval or authorization of the ownership or operation of the capital assets of such electric and gas-utility companies by a single company, unless the State Commission of such State shall expressly approve such holding company having such interests." [74th Congress, 1st Session, Senate Bill 1725, Sections 8(b) and 8(d) and House Bill 5423, Sections 7(b) and 7(d).]

In commenting upon the latter provision the Senate Committee stated (74th Congress, 1st Session, Hearings before the Committee on Interstate Commerce, U. S. Senate, p. 56):

> "This subsection is concerned with competition in the field of distribution of gas and electric energy—*a field which is essentially a question of State policy* and becomes the proper subject of Federal action only where the extra-State device of a holding company is used to circumvent State policy." [Italics supplied.]

Then, referring to the first point noted above, the report continued:

> "The preceding subsection (b) however, is concerned with the sources of natural gas and the transportation of that gas in interstate commerce (Questions which are essentially national in scope * * *)."

The comments of the House Committee with respect to the identical provisions in House Bill 5423 were entirely in accord with those of the Senate Committee (74th Congress, 1st Session, H. of R., Committee on Interstate and Foreign Commerce, Hearings, page 330). At the time the original bills were introduced, therefore, the Congressional intent with respect to the operation of

gas distribution systems together with electric systems was to leave that question where it was, in the hands of the individual States, and merely to direct the Commission not to contravene the policies established by the States.

Although the provision relating to production and transmission of natural gas was eliminated from subsequent versions of the bill, the provision making it unlawful for a holding company to acquire control of an electric utility company and a gas utility company[12] serving substantially the same territory in contravention of State policy was continued and later became Section 8 of the Act.

The history of the Act evidences no intent on the part of Congress to raise a presumption against the retention of existing common control of a gas system and an electric system or in favor of independent ownership of such systems. The Commission itself has recognized that Congress left the matter to the States:

> "The question of public policy as to the common ownership of gas and electric facilities in the same territory is apparently left by the statute to the decision of the States (see Section 8)." *American Water Works and Electric Company, Inc.* 2 SEC 972, 983, note 3 (1939).

The decision of the Commission in this case indicates that it now regards the question of common ownership of gas and electric facilities in all its phases as a Federal question within its competence under Section 11(b)(1)(A).

In *The United Gas Improvement Company*, 9 SEC 52, 81, 82 (1941), the Commission in holding that gas and electric properties together could not constitute a single system, stated:

> "Although it is true that the Congressional discussions during the period in which the bills took

[12] Under the Act a gas utility company is limited to one which owns or operates distribution facilities. See Section 2(a)(4).

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this form [early versions] indicate that the language was intended to permit the retention of both gas and electric properties within the 'single geographically and economically integrated public utility system,' this must be considered in the light of the fact that no provision was made at that time for the retention of additional systems."

Senator Wheeler indicated that the Holding Company Act in final form was intended to be more flexible as to retainable properties than were the earlier versions of the bill.[13] If Senator Wheeler was right, the Commission's construction of Clause (A) is wrong, because, so construed, its impact would appear to be more onerous than the provisions of the bill before its final revision would have been.

(c) There is no basis in fact for an inference that the effect of independent ownership of gas and electric services is *necessarily* beneficial.

The assumption that in every instance there is a *danger* of suppression disregards many relevant factors. Among these are the existence of State regulatory authorities which fix the standards of service and the conditions under which service is to be extended to any one who requests it, the existence of effective consumer demand, and the fact that the States through their regulatory commissions, if they deem it in the public interest, may fix the net return available to common stockholders of the utility company at exactly the same rate for each additional dollar invested, whether it be in facilities for gas or for electric service.

Similarly the *danger* that one service will bear burdens properly allocable to the other is immaterial in the absence of evidence that the expenses allocated to each service under combined operation do not exceed the estimated expenses of the same service under independent opera-

[13] 79th Cong. Record 14479, August 24, 1935.

tion. When, as here, only a single operating company is involved, the question of allocation of expenses is strictly a matter of State regulation.[14]

The Commission cites in its brief the opinions of two State Commissions in reference to particular companies for the proposition that the effect of joint ownership of gas and electric properties on gas properties has been the subject of some concern to State utility commissions.[15] The mere expression of concern on such a controversial subject by two State Commissions, made in reference to particular companies not here involved, clearly cannot be the basis of a general inference under Clause (A).[16] Such statements have no greater relevance to the issue than general statistical comparisons of independent and combination companies. In *North American Company* (Holding Company Act, Release No. 5657; March 15, 1945), the Commission, after discussing certain comparative studies purporting to show the relative merits of independent operation, stated (at p. 7):

> "However, we have some doubt as to the relevance, even of a well made study, on the specific cause here presented. The unique problems of operation of individual companies make comparability a difficult

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[14] It may be noted that the allocation question is not eliminated by separation of gas and electric services, since the problem of fixing rate schedules for different classes of consumers receiving the same service, whether electric or gas, involves the allocation of production and the transmission expenses of the particular service, as well as of general and administrative expenses, which is an exceedingly more complex problem than the allocation of the latter between gas and electric services.

[15] *Helena Light & Railroad Company*, PUR 1920 D. 668 (Mont.); *Twin State Gas & Electric Company*, 25 NHPS Com. Rep. 277 (1943).

[16] The opinion of State Commissions is not uniform in this respect. In fact, at the Hearings before the Senate Committee on Interstate Commerce on April 29, 1935 (p. 783), the General Solicitor of the National Association of Railroad and Utility Commissioners testified that "There is not anything in the nature of things so inimical to the public interest in such common holdings".

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matter, at best. Further, the relevant issue is whether *the particular company* will do better if independent." (Italics the Commission's.)

The Power Committee of the Twentieth Century Fund notes that the Commission "has indicated a tendency to insist upon the desirability of 'free and unrestrained' competition as between gas and electric service in a given area to the point of creating a heavy presumption against the retention of combined electric and gas operations". The Committee then remarks that "It is not clear that Congress in the Holding Company Act attempted thus to solve one of the most controversial questions in the whole field of public utility economics".[17]

The Solicitor General of the National Association of Railroad and Utility Commissioners, appearing on behalf of the State Commission membership of the association, made the following statement before the Senate Committee on Interstate Commerce at the hearings on the Holding Company Bill on April 29, 1935 (p. 783):

> "The judgment of our people was that the instances where there are these common holdings are very numerous, and that there is not anything in the nature of things so inimical to the public interest in such common holdings as to make it desirable to have a provision of law which outlaws them. You are setting up a commission here to regulate electric utilities. If it finds that this common holding is sufficiently opposed to the public interest so that there ought to be some limitation on it, we assume that it would so report to Congress, and secure legislation. But we have not any information which leads us to believe that this provision ought to be in the law, which would absolutely outlaw all common holdings. I might state that in the city of Keene the gas company was prac-

[17] *The Power Industry and the Public Interest*, The Twentieth Century Fund, 1944, pages 251-252.

tically dead until the people who are running the electric company reached out and acquired it, and put in new gas manufacturing machinery, and gave a good gas service. I know that in that community they did a good service."

The Right Honorable Major G. Lloyd George, British Minister of Fuel and Power, has been quoted as saying in March, 1943 that:

"gas and electricity had had many tussles, but now there must be cooperation between them. *We would not get the best if there were an internecine struggle.* The two industries must be complementary—not antagonistic. With such co-operation we could look forward to the future with confidence." (Italics supplied.)[18]

The view of the British Gas Federation, on this subject has been stated as follows:[19]

"The objective of all the fuel industries is service to the community. By hostile competition and retaliatory measures directed against each other, much damage can be done to the final prejudice of the user. Competition between gas and electricity was acute before the War in the heating field (*e. g.* cooking) in which gas had replaced coal. If gas were to be displaced by electricity on a substantial scale in this field, it would—on the reduced average consumption per consumer—result in average gas costs rising, whilst the ability to offer lower prices for additional supplies of gas would tend to disappear. Moreover, such displacement—by reason of the heavy and possibly uneconomic expenditure involved to meet

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[18] Quoted in the Report of the British Gas Federation on the Planning of the Gas Industry; October 1943, page 11.

[19] Report of British Gas Federation on the Planning of the Gas Industry; October 1943, pages 11-12.

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the load factor—would prove embarrassing to the electricity industry.

* * * *

"Owing to the absence of electrical storage, the problem of the load factor is more critical in the case of electricity than gas. By way of illustration, if all gas consumers in a town simultaneously boiled kettles all the gas required could be taken from storage with no direct call upon the Gas Works. Without such storage this peak demand would require a Works at least five times the size, costing over twenty times as much as a gasholder. By careful selection and control of the heating loads met by electricity, to ensure that they remain off-peak, considerably more than the present electrical output should be available at low prices on present plant and distribution systems, balanced by the increased use of low-priced gas for those many purposes which, without storage, represent a high daily peak."

There is American authority as well for the contention that basically gas and electric services are generally almost completely complementary, the sphere of effective competition being very limited. The complementary character of the two services is readily apparent from the technological characteristics of gas and electricity:

"Energy in the form of fuels can be converted into useful heat with a high degree of efficiency even when including the conversion losses from coal to gas. However, where the energy in fuels is converted into energy able to do work, *i. e.*, electricity or mechanical energy, large losses of the order of 75% are involved, whether the conversion is made by gas engine, boiler and turbine or any other known means of conversion. Now to take such energy which has experienced such heavy losses and convert it back into heat to supply heat requirements, which could otherwise be supplied direct from fuels without these losses, is not economic.

In general, therefore, *where heat is required, some two or three times the amount of useful energy can be made available to a customer in the form of gas from a given amount of coal, as can be made available in the form of electricity.* Where light and power are concerned, both forms of energy are subject to these same heavy losses and electrical transmission for light and power needs has definite fundamental advantages, due to ease of application, lack of reciprocating parts, freedom from noise, etc."[20]

Thus the desirability of competition between electric and gas services and the extent to which such services are in fact complementary rather than competitive involves highly controversial questions. One thing only is certain, namely, that in industries employing such a large proportion of fixed assets as does the utility industry, competition which is not restrained within economic limits is destructive, and ultimately results in impairment of service to consumers and loss to investors. The whole history of the electric and gas utilities testifies to this.

II. Clause (A) as interpreted by the Commission prescribes a vague and meaningless standard.

(a) Congress intended Clause (A) to afford a definite, concrete and effective standard for the guidance of the Commission and the companies.

The conference report on the substitute bill which was finally enacted clearly indicates the intention of Congress to provide a *definite, concrete,* and *effective* standard for the guidance of both the Commission and the companies (H. of R. Report No. 1903, 74th Cong. 1st Sess., pp. 70-71):

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[20] *"Time Marches On." Where is Manufactured Gas Marching?* by A. M. Beebee, American Gas Association, 1938, Technical Section, Gas Production Committee, page 5. Mr. Beebee is General Superintendent of Rochester Gas & Electric Corporation, a combination gas and electric operating company, which is an indirect subsidiary of the Trustees of Associated Gas and Electric Corporation.

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"The conference substitute meets the House desire to provide for further flexibility by the statement of additional *definite and concrete circumstances* under which exception should be made to the form of one integrated system. *Definite exceptions* not only provide a satisfactory constitutional standard but also *an effective standard* for the guidance of both the Securities and Exchange Commission and those holding companies which wish voluntarily to comply with Congressional policy.

"The substitute, therefore, makes provision to meet the situation where a holding company can show a real economic need on the part of additional integrated systems for permitting the holding company to keep these additional systems under localized management with a principal integrated system. Under such circumstances the Commission is directed to permit the holding company to retain control of such additional systems, even though not physically integrated with the principal system, provided all such integrated systems are located in the same State or States, or in adjoining States or a contiguous foreign country." (Italics supplied.)

Senator Wheeler also indicated that Section 11 was intended to provide a concrete and effective standard (79th Cong. Rec. 14479, August 24, 1935):

"Section 11 in the Senate bill as you will recall, required that a holding company limit its operations to one integrated operating system and to businesses reasonably incidental thereto. The House bill also purported to limit the operation of a holding company to one integrated system, but permitted an exception which allowed the Commission to permit a holding company to control as many systems as it deemed consistent with the public interest. The House bill accordingly thrusts the entire burden of breaking up the giant holding companies upon the Securities

Commission *without any effective or constitutional standard to guide them* in their task and with no concrete congressional sanction to fall back upon to resist pressures that would inevitably be brought against the Commission to prevent their taking any effective action. Since both bills accepted the proposition that a holding company should normally be limited to one integrated system, my colleagues and I conceived it to be our task to find what *concrete exceptions*, if any, could be made to this rule that would satisfy the demand of the House for some greater flexibility. After considerable discussion the Senate conferees concluded that the farthest concession they could make would be to permit the Commission to allow a holding company to control more than one integrated system if the additional systems were in the same region as the principal system and were so small that they were incapable of independent economical operation and if the combination of these small systems under one holding company would not create a corporation so large as to impair the advantage of localized management and the effectiveness of regulation. I consider this a very generous concession on the part of the Senate. If properly administered, however, this concession should not defeat the purpose of the President to break up the giant holding companies with their undue concentration of economic power and with their absentee management by remote control." (Italics supplied.)

The conferees, therefore, added Clauses (A), (B) and (C) to Section 11(b)(1) in order to indicate "definite and concrete circumstances" under which additional systems might be retained and such "definite" and "concrete exceptions" were intended to provide "an effective standard for the guidance of both" the Commission and the companies.

In fact, if Congress did not have in mind increased operating expenses and similar costs as constituting a loss of

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economies it is difficult to conceive what it did have in mind. How else can "economies" arise if not by reason of joint use of administrative and other personnel and of equipment or facilities? If substantial economies of this character, cannot, standing alone, satisfy the requirements of Clause (A), then we must conclude that Clause (A) and, therefore, the entire provision for additional systems under Section 11(b)(1), is meaningless.

(b) The Commission has read into Clause (A) a type of limitation on the extent of holding company systems which Congress provided for only in Clauses (B) and (C).

At page 85 of its brief, the Commission refers to the testimony of the Company's witnesses that independent operation would result in certain increased costs:

> "However specific in dollar figures is the opinion testimony of Company witnesses, it amounts in substance to nothing more than a repetition of the dubious economic philosophy which Congress had rejected in adopting the Act, namely, the argument of holding company managements that economy of operations in the industry had been advanced by indefinite expansion of the holdings under a single management, and that any contraction would necessarily result in a loss of economies."

Congress did reject the philosophy that *indefinite* expansion produces economy of operation when it permitted holding companies to retain a single integrated system and additional systems only within the specific limitations provided by Clauses (B) and (C) of Section 11(b)(1). Clearly Clauses (B) and (C) provide definite limits to the number of retainable additional systems apart from the question of loss of economies. These two clauses prevent *indefinite* expansion. Clause (A), on the other hand, is a concession by Congress to the contention that "contraction would * * * result in a loss of economies." Since Congress did not wish to make a complete concession on

this point, it placed a limit, by means of Clauses (B) and (C) on the additional systems that might be retained upon a showing of loss of substantial economies. Clauses (B) and (C) define the limits upon the scope and size of holding company systems which Congress deemed necessary in the public interest, because where those limits were exceeded the disadvantages to consumers and investors from great concentrations of economic power were believed to outweigh any conceivable loss of economies. Under Clause (A), however, the dollar loss of economies to consumers and investors was intended as the sole consideration.

(c) The Commission has been inconsistent in its interpretation of the words "substantial economies".

The Commission contends in its brief (p. 81) that Congress expected "that a company able to stand alone—*i. e.*, capable of managing its own affairs—was to be given its independence even if relatively small in size".[21] It

[21] It is possible to infer from two of the Commission's most recent decisions that it is interpreting the words of Clause (A), "cannot be operated as an independent system" as permitting it to consider not whether a system is "able to stand alone", but whether such system might be combined with other properties, the result of the new combination being to regain, at least from the standpoint of consumers, the economies lost by separation from the principal system. Thus in *The North American Company* (HCA Release No. 5707, p. 13, April 9, 1945) the Commission criticized the respondents therein for having been "unmindful of the possibility that new operating alliances and resulting economies may be achieved". Again in *Peoples Light and Power Company* (HCA Release No. 6000, p. 24, August 23, 1945) the Commission declared: "It may well be that the LaGrange properties, after severance may be operated in combination with other properties so as to secure beneficial effects comparable to those claimed to be obtained under Peoples' control." Perhaps Congress might have given the Commission power to compel combinations. Clearly it did not do so. Against this background the word "independent" in Clause (A) cannot properly be construed as having any reference to the possibility of "new operating alliances". The Commission has not indicated in its brief in this case that any such considerations operated in this case. We cite the foregoing opinions of the Commission merely to indicate the extent to which the Commission seems to have gone in order to justify requiring separation of gas and electric properties under Clause (A).

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does this in reliance on the statement of Senator Wheeler quoted above. The difficulty is that the Act itself does not indicate that a company, to be retainable under Clause (A), must be either unable to stand alone or be a small company. Had that been the intention it could easily have been expressed.

Nor has the Commission so interpreted Clause (A) except when considering a combination of gas and electric properties. In *Columbia Gas and Electric Corporation* (HCA Release No. 5455; December 1, 1944) the Commission allowed retention of three clearly substantial groups of gas properties (Charleston, Pittsburgh and Columbus groups) under the standards of Section 11(b)(1)(A), (B) and (C) of the Act. These three groups had gross utility plants of approximately $139,000,000, $101,000,000, and $117,000,000, respectively.

In order for the Commission to hold that a group of gas properties (not owned by the same company) constitutes an integrated gas utility system as defined by Section 2(a)(29)(B), the Commission must make, in effect, the very same findings which it would have to make under Clauses (A), (B) and (C) of Section 11(b)(1), including a finding that substantial economies result from coordinated operation. In considering substantial economies under Section 2(a)(29)(B), however, the Commission does not appear to have evinced any concern about size, and has in fact found that gas properties constituted a single system under Section 2(a)(29)(B) on the basis of the very type of evidence which it has found to be insufficient under Clause (A) to prevent severance of gas and electric prop-

erties.[22] Clearly there is no basis in the Act, nor has the Commission suggested any, for applying a different meaning to the words "substantial economies" in these two Sections.

III. The Commission cannot refuse to find "the loss of substantial economies" on a basis *dehors* the record before it.

The Commission has offset intangible and undeterminable future "beneficial effects of independent ownership" of gas and electric services against dollar and cents estimates of losses of economies resulting from the severance of such services. Manifestly if the Commission can do this, in no case is it possible for a reviewing court to determine whether

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[22] In *The North American Company* (HCA Release No. 5657; March 15, 1945) the Commission stated in holding two gas properties to constitute a "single integrated gas utility system" (p. 6):

> "Significant evidence, not heretofore available to us, has been introduced to show that the combined operation of Peoples and Argus under Northern control results in substantial economies which would be unavailable upon separation. A large portion of the claimed increase in Argus' operating expenses which would result from divestment is attributable to administrative and general expenses."

In *Cities Service Company* (HCA Release No. 5028; May 6, 1944), the Commission stated (p. 7):

> "The three companies have substantially the same management. The Central offices of Gas Service and Kansas City Gas are located in the same building in Kansas City, Missouri, while the Central offices of Wyandotte are in Kansas City, Kansas, three miles away. The three companies have the same president, treasurer, assistant treasurer, counsel, and new business manager, and there are four interlocking directors. In purchases, construction, advertising, and exchange of ideas, the companies are operated as a single enterprise. They are all serviced by Gas Advisers, Inc., a mutual service company in the Cities Service System. Counsel for our Public Utilities Division concedes, and, on the basis of the evidence as to size, methods of operation and location we find, that the three companies form an 'integrated public-utility system' as defined in Section 2(a)(29)(B) of the Act."

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or not the Commission "was obliged to make the prediction that substantial economies would in fact be lost by divestment," (Commission Brief, p. 91), since the Commission itself finds it impossible to state even in terms of rough approximation what, if anything, those effects might be. Certainly the burden of proof is on the Company to establish that substantial economies would be lost. However, once the Company has presented credible evidence, the Commission must either hold that the showing made by the Company in and of itself does not establish loss of substantial economies, or go forward with evidence to establish offsetting benefits of independent operation. The Commission contends that here the Company failed to make its case (Commission Brief, p. 77, note 38). If this was the situation, then the Commission's reference to the "beneficial effects" of independent operation was at best intended as a guide to the questions to which additional evidence should be addressed. The trouble is that the Commission's view requires the Company to prove a negative, namely, that the "beneficial effects" of independent ownership will *not* be present in the case before it, a matter which the Commission itself recognizes as "not readily susceptible of absolute proof" (Commission Brief, p. 90)

After all, the Commission has here ordered the taking of a drastic step, namely, the disruption of an existing operating company by divestment of its gas business. It has done this not upon the evidence before it, but clearly on the basis of its conviction which, if founded upon fact, has basis only in facts *dehors* the record. This Court has many times refused to sanction such procedure by an administrative body.

We quote Mr. Justice Brandeis in *Baltimore & Ohio Railroad Company* v. *U. S.* (The Chicago Junction Case), 264 U. S. 258, 263:

> "Facts conceivably known to the Commission but not put in evidence will not support an order."

See also:

Interstate Commerce Commission v. *Abilene & Southern Railway Company*, 265 U. S. 274;

Ohio Bell Telephone Company v. *Public Utilities Commission of Ohio*, 301 U. S. 292.

Conclusion.

Clearly Congress did not invest the Commission with power to determine the broad question of public policy as to whether independent or combination gas and electric service is desirable. That question was left for determination by the individual States. Congress did on the other hand, direct the Commission to permit the retention of additional systems upon proof that independent ownership of such additional systems would result in "loss of substantial economies", subject, however, to the limitations provided in Clauses (B) and (C) of Section 11(b)(1) of the Act. In setting up the standard of "loss of substantial economies", which Congress intended to be a definite, concrete and effective standard, Congress recognized that such standard could be met by properties which, although they could not meet the requisites of an "integrated system", achieved economies in operating and other expenses by reason of the fact that certain functions were conducted jointly for the entire group of properties. Congress recognized that in such instances, depending upon the extent of jointly conducted functions, severance of such properties would result in increased expenses, and Congress also recognized that such expenses would constitute the principal, if not the only, proof of "loss of substantial economies". Against this background it is clear that the decisions below directed divestment of "Virginia Gas" because Engineers Public Service Company failed to prove the negative of the Commission's unwarranted assumption that the effects of independent ownership would be necessarily beneficial—an assumption which has no basis in the record.

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In these circumstances, we respectfully submit that the question whether "Virginia Gas" is retainable together with "Virginia Electric" should be remanded to the Commission for further findings consistent with the opinion of this Court as to the proper interpretation of "loss of substantial economies" as used in Clause (A).

Respectfully submitted,

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